



Budget and Economic Update

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March 31, 2021

The Big Picture

A sizable budget surplus this year and likely next, then deficits

- An FY 20-21 surplus even without latest federal stimulus (ARP)
- New federal funds available through December 2024 (much is restricted)
- IFO estimates longer-term deficit at ~\$2.5 billion | consensus it is significant

Labor market down, but nearly all other economic indicators strong

- Down 441k jobs in February from prior year
- Positives: housing market, sales tax revenues show strong growth

Minimum wage, PIT changes and combined reporting/rate reduction

- Minimum wage impact looks very different now than 2019
- Combined reporting vs rate reduction: what is the trade off?

General Fund Financial Statement (Jan 2021)

| | 19-20 | 20-21 | 21-22 | 22-23 | 23-24 | 24-25 | 25-26 |
|------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Beginning Balance | \$30 | -\$2,734 | -- | -- | -- | -- | -- |
| Current Year Revenues | 32,276 | 38,437 | \$36,675 | \$37,851 | \$39,352 | \$40,828 | \$42,321 |
| Less Refunds | <u>-1,150</u> | <u>-1,300</u> | <u>-1,326</u> | <u>-1,353</u> | <u>-1,380</u> | <u>-1,407</u> | <u>-1,435</u> |
| Net Revenues | 31,126 | 37,137 | 35,349 | 36,498 | 37,972 | 39,421 | 40,885 |
| State Expenditures | -34,090 | -33,141 | -37,975 | -39,223 | -40,586 | -41,877 | -42,971 |
| Current Year Balance | -2,934 | 1,263 | -2,626 | -2,725 | -2,613 | -2,455 | -2,086 |
| Plus Prior Year Lapses | <u>200</u> | <u>219</u> | <u>125</u> | <u>125</u> | <u>125</u> | <u>125</u> | <u>125</u> |
| Prelim Ending Balance | -2,734 | 1,481 | -2,501 | -2,600 | -2,488 | -2,330 | -1,961 |

Note: Millions of dollars. **Excludes \$900 million in supplemental appropriations for FY 20-21 requested in Executive Budget. For FY 21-22, excludes enhanced FMAP (\$2.4 billion) and new American Rescue Plan stimulus.** Prior year lapses include transfers to Budget Stabilization Reserve Fund. Source: IFO Economic and Budget Outlook, FY 20-21 to 25-26 (Jan 2021).

FYTD Revenues (Adjusted for Delayed Due Dates)

| | Actual Revenues (\$ millions) | | Notes |
|-----------------------|-------------------------------|-------------|---|
| | Amount | Growth | |
| General Fund | \$28,706 | 3.6% | |
| Corporate Net Income | 2,808 | 11.5 | anticipate weak final payments |
| Sales - Non-Motor | 7,958 | 4.2 | strong online growth |
| Sales - Motor Vehicle | 1,316 | 15.4 | pent-up demand |
| Income – Withholding | 8,131 | 0.3 | |
| Income – Other | 3,100 | 8.1 | final quarterly payments strong, includes \$100m from PPP |
| All Tobacco | 891 | 3.7 | |
| Inheritance | 964 | 3.3 | |
| Realty Transfer | 465 | 14.9 | housing market very strong |
| All Other | 3,071 | -3.5 | |

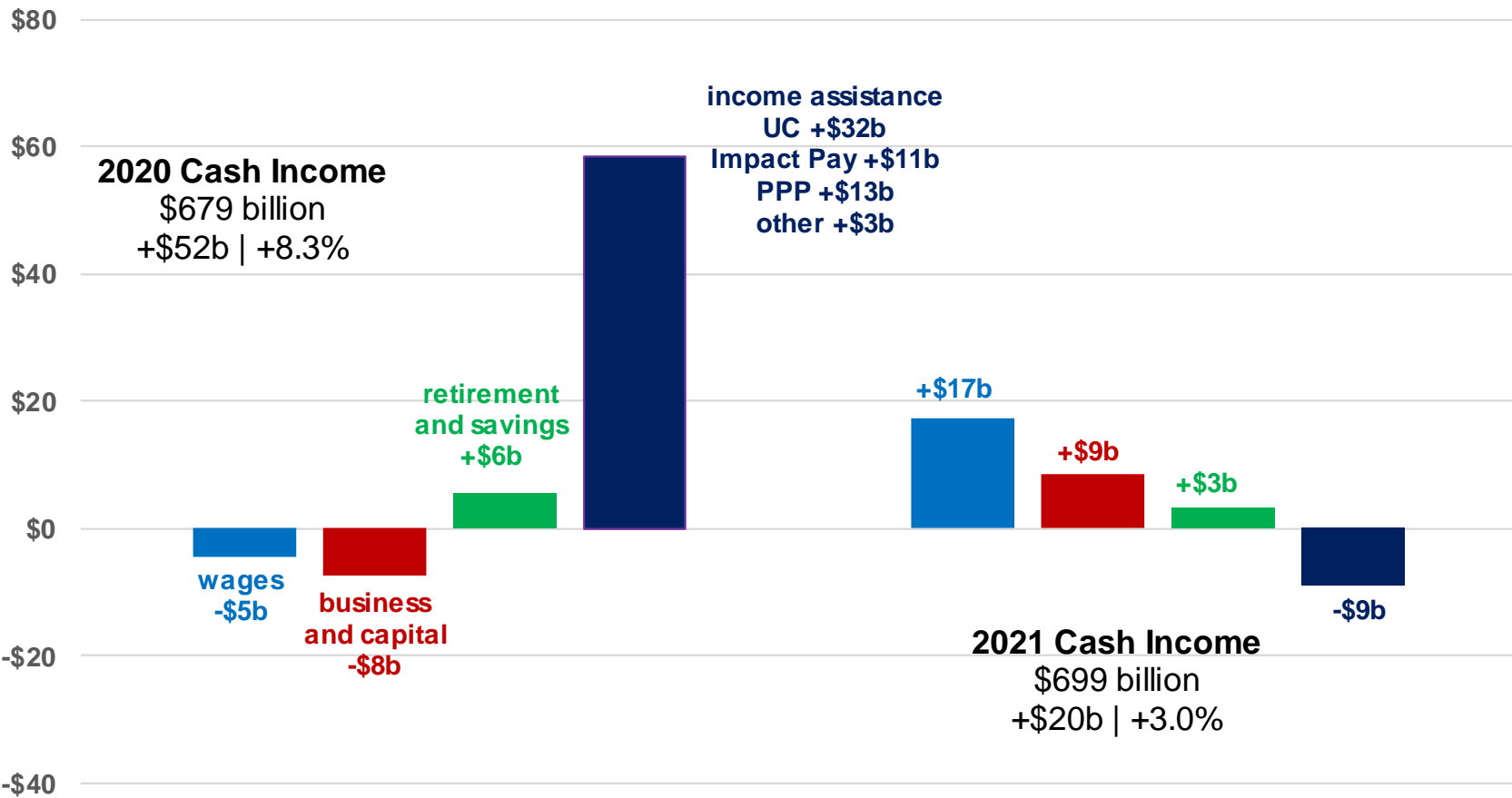
Note: Millions of dollars. Growth rates adjusted to reverse the shift of revenues to FY 2020-21, as well as the impact of one-time transfers and an extra PIT withholding due date in FY 2020-21.

New Round of Federal Stimulus

| | CARES | CAA | ARP | Notes |
|--|-------------|-------------|-------------|-------------------------------|
| Payments to Individuals | | | | |
| State Unemployment Compensation | \$5.2 | \$1.6 | -- | CAA is full year amount |
| Federal Pandemic Unemploy Comp (FPUC) | 16.2 | 3.4 | 4.5 | extended to Sept |
| Pandemic Unemployment Assistance (PUA) | 7.0 | 1.1 | 1.3 | |
| Other Federal Assistance | 3.3 | 0.9 | 1.4 | |
| SNAP Benefits | 0.9 | 0.6 | 0.3 | extended to Sept |
| Economic Impact Payments | 11.0 | 6.3 | 14.7 | ARP at \$1,400 per |
| Child Tax Credit Awards | <u>0.0</u> | <u>0.0</u> | <u>3.6</u> | spread through year |
| Total | 43.6 | 13.9 | 25.7 | |
| Other Federal Programs | | | | |
| Paycheck Protection Program (PPP) | \$20.7 | \$11.2 | \$0.3 | |
| Direct State Support | 6.1 | 4.6 | 18.2 | \$7.3b General Aid |
| Direct Local Support | 2.6 | 0.8 | 9.1 | \$6.1b General Aid |
| Other Support | <u>4.7</u> | <u>0.8</u> | <u>3.3</u> | hospital, college, restaurant |
| Total | 34.1 | 17.5 | 30.9 | |

Note: Figures in dollar billions. CARES is Coronavirus Aid, Relief and Economic Security Act of 2020. CAA is Consolidated Appropriations Act of 2020. ARP is American Rescue Plan of 2021. ARP monies must be spent on costs incurred prior to Dec 2024 and cannot be used to reduce taxes or make pension contributions.

Pennsylvania Cash Income



Recent PA Economic Growth Rates or Change

| | 2020 Q1 | 2020 Q2 | 2020 Q3 | 2020 Q4 | 2021 Q1 |
|----------------------------|---------|---------|---------|---------|---------|
| Real GDP | -5.8% | -34.0% | 35.5% | 3.7% | --- |
| Personal Income | 2.5% | 13.1% | 9.0% | 3.5% | --- |
| Wages-Salaries Paid | 2.2% | -6.2% | -1.0% | -0.2% | 2.3% |
| Sales-Use Tax Revenues | 5.7% | -14.5% | 5.7% | 5.4% | 6.0% |
| Change Payroll Jobs (000s) | 29 | -896 | -517 | -468 | -450 |
| Change Labor Force (000s) | 51 | -96 | -160 | -231 | -229 |
| Home Values | 5.1% | 4.8% | 8.3% | 10.8% | --- |

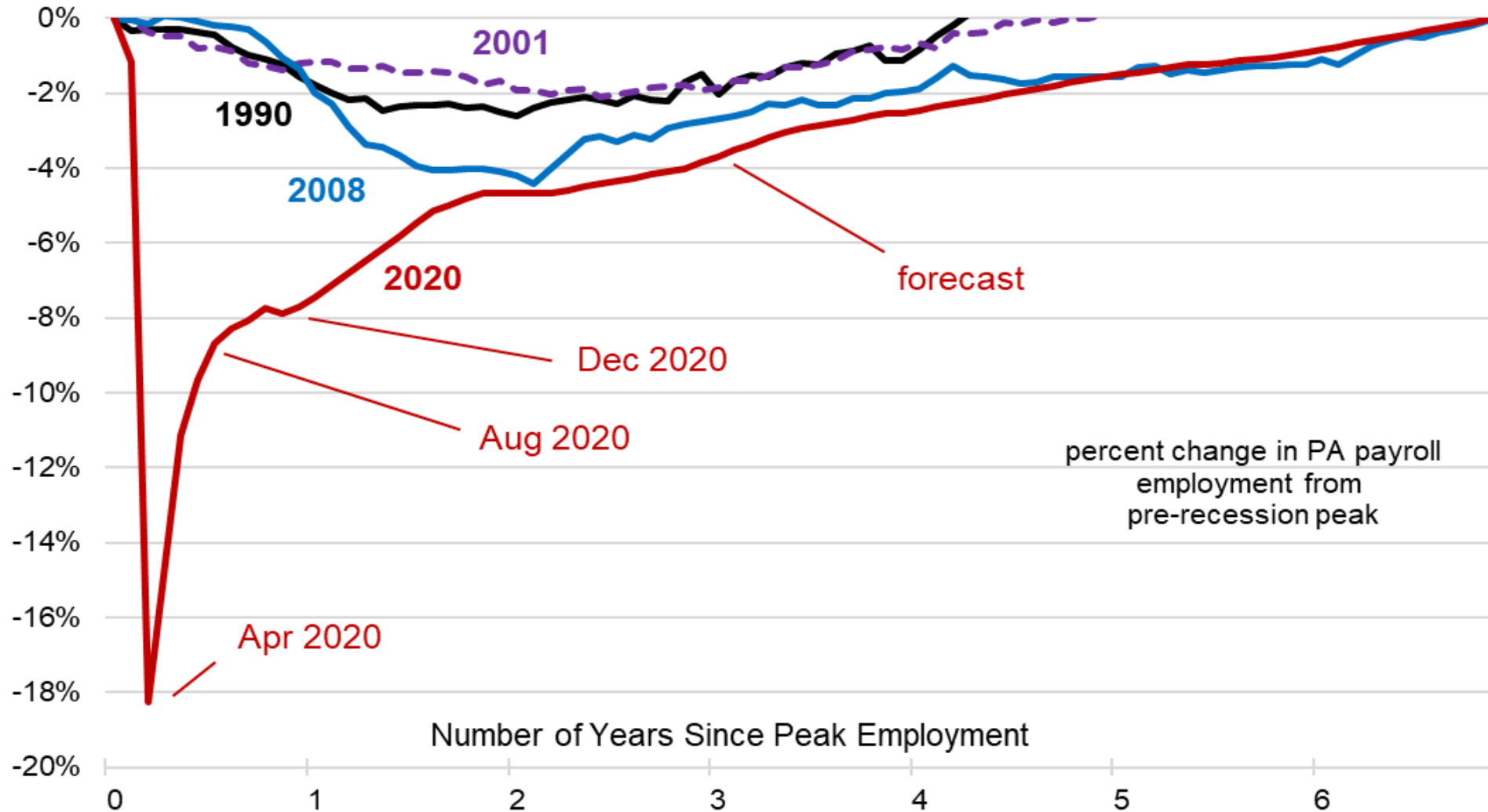
Notes: Real GDP is quarterly annualized growth rate. All other rates are year-over-year. Sales tax adjusts for shifts and transfers. Wages-Salaries growth rate for 2021 Q1 based on withholding tax collections. Change in Payroll Jobs and Labor Force is change from prior year. Labor market data not seasonally adjusted. Data for 2021 Q1 based on January and February.
Sources: U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics, Federal Housing Finance Agency.

Low-Wage and Part-Time Jobs Hit Hardest

| | YOY Number Change (000s) | | YOY Percent Change | |
|-------------------------------|--------------------------|-------------|--------------------|--------------|
| | Apr 20 | Feb 21 | Apr 20 | Feb 21 |
| PA Payroll Employment | -1,099 | -441 | -18.1% | -7.3% |
| Construction | -98 | -10 | -37.9% | -4.1% |
| Manufacturing | -85 | -33 | -14.7% | -5.8% |
| Retail and Wholesale Trade | -172 | -31 | -21.0% | -3.8% |
| Transport and Warehouse | -27 | 1 | -9.0% | 0.3% |
| Financial and Real Estate | -9 | -10 | -2.7% | -2.9% |
| Professional and Technical | -19 | -1 | -5.3% | -0.2% |
| Admin and Waste Management | -68 | -36 | -21.4% | -11.9% |
| Education (excludes local SD) | -37 | -31 | -14.4% | -12.1% |
| Healthcare-Social Assistance | -109 | -49 | -10.3% | -4.6% |
| Arts-Entertainment | -56 | -30 | -59.5% | -35.4% |
| Accommodation-Food Service | -276 | -115 | -57.7% | -24.7% |
| Other Services | -95 | -36 | -36.5% | -13.8% |
| All Government | -25 | -44 | -3.4% | -6.1% |
| All Other | -23 | -17 | -9.3% | -7.1% |

Note: Data are not seasonally adjusted. Figures for January are preliminary. YOY is year-over-year. **Excludes self-employed.**
Source: U.S. Bureau of Labor Statistics, CES State and Metro Area Employment.

IFO Forecast: 6 Years Needed for Full PA Jobs Recovery



Reasons Why Lost Jobs Will Not Return Soon

Labor productivity (output per hour) surged in 2020

- Automation | release less productive employees | working more

Dramatic shift in consumer spending patterns

- Online sales tax collections double | shift to larger firms with online presence
- For example: retail clothing store employment still down by ~20%
- Investment in the home: gyms, meal preparation, entertainment, remodels

Remote working is here to stay

- Impacts restaurants, dry cleaners, formal/business casual clothing sales
- Gasoline consumption down 10% for FY 2020-21

Businesses tighten belts

- Operations and procurement | travel and meals/entertainment | leased space

State and Local Tax Burden: Rates and Ranks

| Corporate Income | | | Personal Income | | | Sales and Use | | |
|------------------|-----------|-------------|-----------------|-----------|-------------|---------------|-----------|-------------|
| | Rank | ATR | | Rank | ATR | | Rank | ATR |
| DE | 1 | 3.62% | NY | 1 | 5.10% | OH | 17 | 2.80% |
| NY | 4 | 0.83 | MD | 3 | 4.17 | NY | 22 | 2.56 |
| NJ | 6 | 0.73 | DE | 7 | 3.40 | NC | 28 | 2.42 |
| PA | 12 | 0.47 | VA | 12 | 3.07 | WV | 30 | 2.33 |
| MD | 22 | 0.38 | WV | 14 | 2.88 | MI | 37 | 1.99 |
| NC | 27 | 0.35 | NC | 15 | 2.78 | NJ | 38 | 1.97 |
| WV | 33 | 0.27 | OH | 18 | 2.65 | PA | 39 | 1.94 |
| MI | 38 | 0.24 | NJ | 19 | 2.63 | VA | 42 | 1.57 |
| VA | 42 | 0.20 | PA | 20 | 2.62 | MD | 43 | 1.48 |
| OH | 46 | 0.10 | MI | 31 | 2.20 | DE | 48 | 0.11 |
| USw | | 0.40 | USw | | 2.48 | USw | | 2.53 |
| USuw | | 0.44 | USuw | | 2.24 | USuw | | 2.46 |

Note: Average Tax Rate (ATR) is the ratio of the state-local tax revenue to modified state personal income. USw is weighted average. USuw is unweighted average (each state has same weight). Total Taxes excludes any severance tax or impact fee.

Source: *State and Local Tax Revenues: A 50 State Comparison*, IFO (November 2020).

State and Local Tax Burden: Rates and Ranks

| | Property | | Liquor, Tobacco, Game | | | Total Taxes | | |
|-----------|-----------|-------------|-----------------------|----------|-------------|-------------|-----------|--------------|
| | Rank | ATR | Rank | ATR | Rank | ATR | | |
| NJ | 3 | 4.96% | WV | 1 | 1.02% | NY | 1 | 14.86% |
| NY | 6 | 4.42 | DE | 4 | 0.72 | NJ | 7 | 11.65 |
| MI | 20 | 3.01 | MD | 5 | 0.66 | DE | 8 | 11.57 |
| VA | 21 | 2.98 | PA | 6 | 0.66 | MD | 10 | 11.20 |
| PA | 25 | 2.82 | NC | 10 | 0.51 | WV | 11 | 11.10 |
| OH | 26 | 2.79 | MI | 13 | 0.48 | PA | 21 | 10.24 |
| MD | 27 | 2.76 | OH | 15 | 0.45 | OH | 25 | 9.91 |
| WV | 36 | 2.35 | NY | 27 | 0.36 | VA | 29 | 9.50 |
| NC | 41 | 2.16 | NJ | 28 | 0.36 | NC | 31 | 9.48 |
| DE | 47 | 1.75 | VA | 38 | 0.26 | MI | 32 | 9.25 |
| USw | | 3.05 | USw | | 0.35 | USw | | 10.20 |
| USuw | | 2.98 | USuw | | 0.40 | USuw | | 9.95 |

Note: Average Tax Rate (ATR) is the ratio of the state-local tax revenue to modified state personal income. USw is weighted average. USuw is unweighted average (each state has same weight). Total Taxes excludes any severance tax or impact fee.

Source: *State and Local Tax Revenues: A 50 State Comparison*, IFO (November 2020).

Minimum Wage Impact: 2019 vs 2022

| Non-Tipped Workers | Number of Payroll Employees (000s) | | |
|--|------------------------------------|--------------|-------------|
| | 2019 | 2022 | Change |
| \$7.25 to \$7.99 | 78 | nominal | -78 |
| \$8.00 to \$9.99 | 428 | 310 | -119 |
| \$10.00 to \$10.99 | 260 | 250 | -11 |
| \$11.00 to \$11.99 | 278 | 205 | -72 |
| \$12.00 to \$14.99 | 764 | 696 | -68 |
| \$15.00 or more | <u>3,916</u> | <u>4,065</u> | <u>149</u> |
| TOTAL | 5,725 | 5,526 | -198 |
| Directly Affected by \$12 Minimum Wage | 1,044 | 765 | -279 |
| Directly Affected by \$15 Minimum Wage | 1,808 | 1,461 | -347 |
| Total Tipped Workers | 177 | 147 | -30 |

Note: Excludes self-employed. Source: Occupational Employment Statistics (OES), 2019.

Combined Reporting and Rate Reduction: Net Tax Cut

| | 20-21 | 21-22 | 22-23 | 23-24 | 24-25 |
|--------------------|--------------|---------------|---------------|---------------|-----------------|
| Combined Reporting | \$66 | \$324 | \$432 | \$411 | \$417 |
| Rate Reduction | <u>-\$75</u> | <u>-\$336</u> | <u>-\$651</u> | <u>-\$945</u> | <u>-\$1,205</u> |
| Total | -\$9 | -\$12 | -\$219 | -\$534 | -\$787 |

Notes

Rate reduction phased in to 5.99% over 5 years

27 states use Combined Reporting

2 of them have an NOL cap (CT at 50%, NH at \$10m)

IFO projects Combined Reporting expands tax base by 12%

DOR projects it is 29%; 5% of firms pay entire increase

Note: Figures in dollar millions.

Source: Independent Fiscal Office, Analysis of Revenue Proposals (April 2020).

Natural Gas Trends

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|------------------------------|----------|----------|----------|----------|----------|----------|
| PA Production (bcf) | 4,601 | 5,096 | 5,364 | 6,123 | 6,815 | 7,090 |
| Growth Rate | 13.0% | 10.8% | 5.3% | 14.1% | 11.3% | 4.0% |
| New Horizontal Wells Drilled | 784 | 501 | 811 | 777 | 614 | 475 |
| Growth Rate | -42.7% | -36.1% | 61.9% | -4.2% | -21.0% | -22.6% |
| PA Natural Gas Spot Price | \$1.37 | \$1.47 | \$2.10 | \$2.59 | \$2.10 | \$1.38 |
| NYMEX Natural Gas Price | \$2.66 | \$2.46 | \$3.11 | \$3.09 | \$2.63 | \$2.08 |
| Impact Fee Collections | \$187.7 | \$173.3 | \$209.6 | \$251.8 | \$200.4 | \$144.9 |
| Wells Paying Impact Fee | 7,874 | 8,121 | 8,518 | 10,164 | 10,112 | 10,438 |
| Average Fee Per Well | \$23,838 | \$21,340 | \$24,607 | \$24,774 | \$19,818 | \$13,882 |

Notes: Production and drilling amounts from DEP. PA spot price is a weighted annual average at major Pennsylvania hubs. NYMEX price is the annual average price of natural gas near-month settlements on the New York Mercantile Exchange, upon which the Impact Fee schedule is based. Impact Fee collections in millions of dollars, reported by the PUC, with 2020 estimated by the IFO. Average Fee Per Well computed by the IFO.

Impact Fee Effective Tax Rates

| Calendar Year | Impact Fee Revenues ¹ | Unconventional Production (bcf) ² | Price of Gas (mcf) ³ | Market Value ⁴ | Annual ETR |
|---------------|----------------------------------|--|---------------------------------|---------------------------|------------|
| 2015 | \$187,712 | 4,601 | \$0.64 | \$2,951,600 | 6.4% |
| 2016 | 173,259 | 5,096 | 0.75 | 3,844,900 | 4.5 |
| 2017 | 209,557 | 5,364 | 1.40 | 7,505,000 | 2.8 |
| 2018 | 251,831 | 6,123 | 1.90 | 11,653,300 | 2.2 |
| 2019 | 200,365 | 6,815 | 1.38 | 9,407,600 | 2.1 |
| 2020 | 144,850 | 7,090 | 0.63 | 4,478,600 | 3.3 |

Notes:

1 Fees in thousands of dollars, reported by the PUC. 2020 is estimated by the IFO.

2 Production data from DEP, in billion cubic feet.

3 Weighted average of spot prices at major PA hubs. Net of post-production costs, assumed to be \$0.80 per mcf based on investor presentations for several regional producers.

4 Does not include natural gas liquids, thousands of dollars.

2020 Energy Impact: Consumption Decline

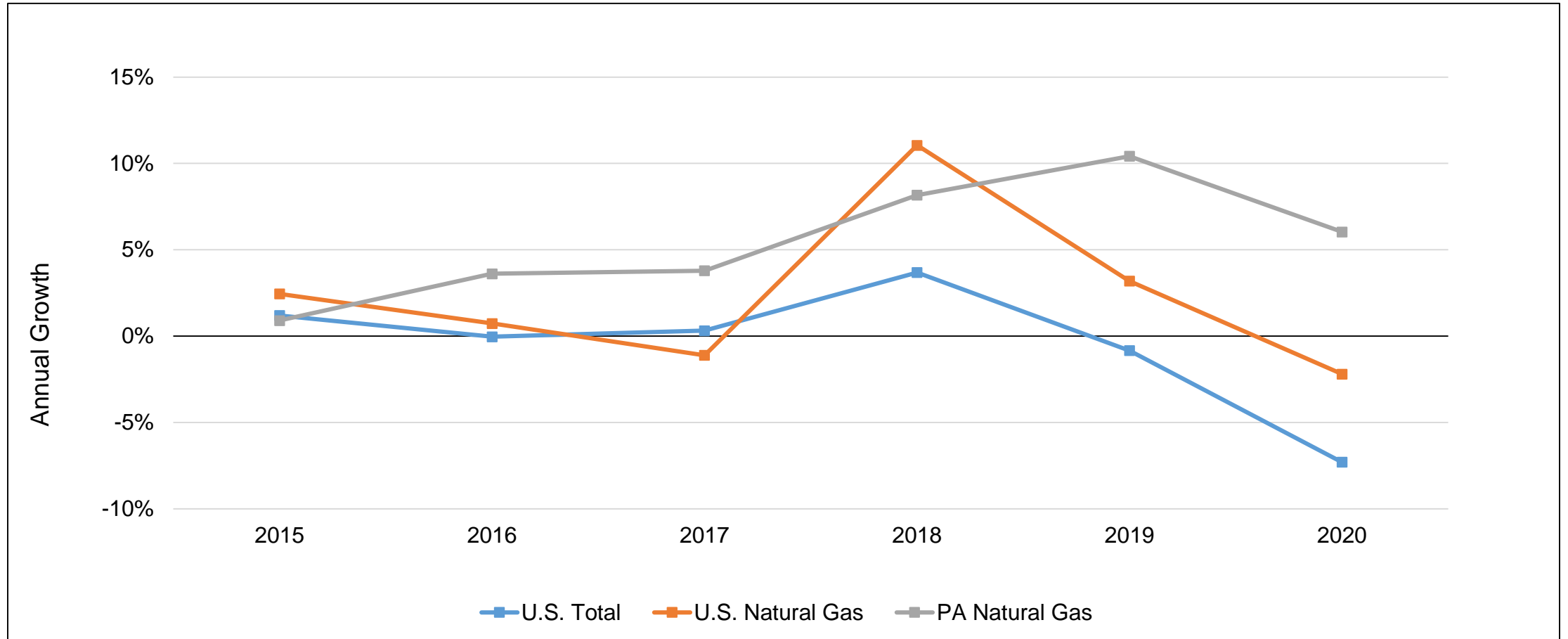
Total U.S. energy consumption down 7 percent year-over-year

- Largest reduction in over a decade, largely driven by coal and petroleum
- Lowest total level of consumption since 2009
- Year-over-year declines in all sources except renewables

After several years of growth, U.S. natural gas consumption falls

- Strongest year-over-year decline since PA became major producer
- PA exports over 75% of the gas it produces, so national consumption is important
- Preliminary data show that in-state consumption grew in 2020

Consumption Growth Trends



Note: U.S. Total includes coal, natural gas, petroleum, nuclear electric and renewables. Source: U.S. Energy Information Administration.

PA Oil and Gas Employment Trends

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | Total Change |
|--|-------|-------|-------|-------|-------|-------|--------------|
| Oil and Gas Extraction | 6,324 | 5,423 | 4,568 | 4,496 | 4,751 | 4,056 | |
| Change | | -901 | -855 | -72 | 255 | -695 | -2,268 |
| Natural Gas Pipeline Transportation | 1,548 | 1,617 | 1,746 | 1,857 | 1,804 | 1,730 | |
| Change | | 69 | 129 | 111 | -53 | -74 | 182 |
| Electric Power Generation – Fossil Fuels | 3,308 | 3,030 | 2,805 | 2,742 | 2,599 | 2,287 | |
| Change | | -278 | -225 | -63 | -143 | -312 | -1,021 |
| Natural Gas Distribution | 4,648 | 4,787 | 4,866 | 4,940 | 4,774 | 4,826 | |
| Change | | 139 | 79 | 74 | -166 | 52 | 178 |

Notes: Electric power generation is related to all fossil fuels, no further detail is available. 2020 employment is as of September. Includes direct jobs only and excludes indirect jobs supported by the industry such as independent contractors.
Source: Bureau of Labor Statistics.

Questions

Presentation posted on the IFO website

<http://www.ifo.state.pa.us/>

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